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PORT OF HOUSTON AUTHORITY

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PORT OF HOUSTON AUTHORITY HOUSTON, TEXAS PHA

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May 16, 2000

Surface Transportation Board
Office of the Secretary
Case Control Unit, ATTN: STB Ex Parte No. 582 (Sub-No. 1)
1925 K Street, NW
Washington, DC 20423-0001

Dear Secretary Williams:

RE:

STB Ex Parte No. 582 (Sub-No. 1)

Major Rail Consolidation Procedures

Comments of the

Port of Houston Authority

on

Advance Notice of Proposed Rulemaking

ENTERED
Office of the Secretary
MAY 16 2000
Part of
Public Record

An original and 25 paper copies of the comments of the Port of Houston Authority in the above-captioned proceeding are enclosed. Also enclosed is a 3.5-inch IBM-compatible floppy diskette containing an electronic copy of the enclosed comments, in or convertible by and into WordPerfect 7.0 format.

Respectfully submitted,

Richard J. Schiefelbein
For: Port of Houston Authority

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The Port of Houston Authority

The Port of Houston Authority ("PHA" or "Port Authority") is an autonomous governmental entity which owns the public facilities along the 50-mile Houston Ship Channel and is the Channel's official sponsor. The Port of Houston Authority owns 43 general cargo wharves, owns and operates the Barbours Cut Container Terminal and leases and operates the Container Terminal at Galveston, which are available for public use. It also owns an export grain elevator, a bulk materials handling plant, a bagging and loading facility, a refrigerated facility, two liquid cargo wharves, and other facilities which are leased to private operators. It is in the early phases of constructing a $1.2 billion container terminal at Bayport on Galveston Bay. The Port of Houston complex also includes numerous privately-owned terminals. The Port Authority also operates the Malcolm Baldridge Foreign Trade Zone.

The Port Authority's facilities handle approximately 15 percent of the approximately 170 million tons of cargo moving through the Port of Houston. The Port of Houston ranks first in the United States in total foreign water-borne commerce handled and second in total tonnage. It is the seventh busiest port in the world. Last year, the Port of Houston handled over 6,500 ships, 100,000 barges and 1,000,000 TEU's (twenty-foot equivalent container units).

The Port of Houston is home to a $15 billion petrochemical complex, the largest in the nation. The Port generates approximately 205,000 jobs and $7.7 billion in economic activity annually.

Changes in the U.S. Railroad Industry

The overall financial health of the U.S. railroad industry in 2000 is far better than it was in 1980 when the Staggers Act was signed and when the current merger rules were promulgated by the Interstate Commerce Commission. In 1980, the railroad industry had substantial excess capacity, a tremendous level of deferred maintenance, poor physical plant, and excessive routings and gateways, all of which resulted in inefficient utilization of resources, poor earnings, and a balkanized network of regionalized railroads. Something clearly needed to be done to restore long-term railroad industry viability. The Staggers Act of 1980 and the associated merger policies were part of the solution. The merger policies established in 1980, reflected in the merger regulations being considered for revision in this proceeding, facilitated the combination of railroads and the elimination of redundancies and inefficiencies in the railroad network. Conditions which had been imposed routinely in earlier merger approvals, particularly those requiring inefficient interchange gateways to be maintained, were eliminated. The railroad industry consolidated and eliminated redundancies and inefficiencies. Financial viability was restored to the industry.

This improvement in the financial health and outlook for the railroad industry did not come without a price. The price of saving the railroad industry has been a tremendous reduction in railroad competition resulting in the virtual elimination of competitive choice for many shippers, including large shippers with multiple locations around the country. The scales were tilted in favor of the railroads in the 1980's and the 1990's, but the time has come for government to take its thumb off of the scales and create a level playing field for the railroads and their customers.

The railroad industry of 2000 bears little resemblance to the railroad industry of 1980. The industry has consolidated to the point where only four major U.S. and two major Canadian railroads remain. Both the railroads and rail customers have made substantial investments in the railroad system, with rail customers making large investments in rolling stock and facilities in order to be able to effectively utilize the railroad network. Although virtually all measures of railroad productivity give proof of the benefits to the railroads of the manner in which the Staggers Act was implemented, these measures mean very little to customers who are captive to a single railroad and can depend neither on competition nor the Surface Transportation Board to assure them reasonable rates and service levels. The railroads have benefited: fewer more efficient through routes have replaced the innumerable through routes required by open gateway requirements, longer single-line hauls have improved transit times and the service abilities of the industry, and extensive use of unit trains and intermodal services have improved railroad efficiency; but the railroad's customers have suffered greatly because of the government's efforts to protect the railroads from competition.

PHA agrees with the Board that the merger regulations and regulatory scheme which may have been appropriate for an industry comprised of numerous regional railroads, many of which were at the time in precarious financial condition, is not the right design for a railroad industry likely to consist of only two railroads, each financially strong and nationwide in scope.

Railroad Competition

While PHA is not uncomfortable with the concept of having only two large nationwide railroads, PHA is uncomfortable with shippers not having competitive choices for shipping their goods.

Two large, financially-strong, nationwide rail systems, each reaching virtually all areas of the country, would have the financial strength to invest adequately in physical plant improvements and equipment, to provide quality service, and to weather the inevitable downturns in economic activity. However, these benefits of a strong, two-railroad system will not be available to many shippers, possibly most shippers, unless effective competitive access to each of the remaining railroads is available to all shippers.

Simply helping the railroads become stronger should not be the objective of U.S. railroad policy anymore. With favorable policies, the railroads have recovered from the financial depths of the 1970's and 1980's and today are financially viable companies, capable and willing to invest in plant and equipment and to operate safely and efficiently.

U. S. railroad policy should recognize that the regulatory policies which protect railroads from rail-to-rail competition and prevent shippers from using competition to assure reasonable service and fair rates need to be changed. The Board has opened discussion on competition and competitive access in its Advance Notice of Proposed Rulemaking. The Port Authority believes the time has come for a fundamental policy change in the regulatory scheme regarding railroad competition, with the objective of assuring competitive railroad rates and service for all shippers who use the U.S. railroad system.

PHA is concerned that the intense concentration in the railroad industry, when combined with regulatory policies that support excessively high rates for shippers and plants captive to a single railroad, works to the long-term detriment of cities like Houston which depend on industrial activity for their economic vitality. Many of the industrial plants in the Houston area, including those in the petrochemical industry, are served by only one railroad. Continuation of the prevailing railroad regulatory philosophy cannot help Houston, but can threaten its future growth by making Houston a less-attractive location for petrochemical production and risking future expansions being located off-shore.

Throughout the history of the U.S. economy, competition among providers of goods or services has proven to be most effective in assuring quality products and services are made available in the marketplace at a reasonable price for customers while providing reasonable profits for efficient producers. In the railroad industry, competition causes railroads to strive to satisfy their customers by providing consistent, reliable service and continuously improving efficiency and reducing costs. Origin and destination competition and competitive routings are key elements of railroad competition.

Origin and Destination Competition. In situations where a plant or facility is served by only one railroad, which is a common situation in the Houston region, the shipper or receiver at that facility does not enjoy the benefits of rail competition. The shipper or receiver is at the mercy of the serving railroad, particularly if the commodity being shipped is not easily diverted to truck shipment. National surveys have consistently shown that shippers who are captive pay an average of approximately 30 percent more for rail transportation than do shippers who enjoy competitive rail service.

Competitive Routings. The Port Authority is concerned that shippers, even those with competitive rail choices at their Houston facilities, may lose those competitive choices as the result of the merger of one of their competitive serving railroads with the railroad serving the destinations for their shipments. Having competitive choices serves these shippers well in terms of rates, car supply, train schedules, and customer service. Even though their origin location would continue to be served by two railroads (a two-to-two point) and the criteria applied in past mergers would indicate no reduction in competition, in reality, these shippers would lose the option of shipping over the competing railroad because the merging railroad would not make competitive rates available from the interchange point to the destination; the reverse would apply for products moving to Houston. The risk that rail mergers may extend existing bottlenecks, further diminishing the competition available to Houston-area shippers, makes the preservation and, where necessary, the creation of competition an important imperative for the Board in crafting the standards by which future railroad mergers will be judged and conditioned.

Recommendations. The Port of Houston Authority recommends that the Board include in its revised merger regulations provisions requiring the creation of rail-to-rail competition where there is none, the preservation of rail-to-rail competition where it exists today, and the preservation of existing competitive routes at reasonable rates.

PHA recommends that the Board revise its merger regulations to require merging railroads to permit competitive access to all shippers located on their lines in major terminal areas and to all shippers on their lines located within a pre-determined distance from a railroad interchange point. Further, the Board should require that merging railroads, now that the railroads are few in number and principal routes are well-established, to maintain existing gateways and existing joint line rate levels at those gateways, subject to an annual indexing administered by the Board.

How these recommendations are implemented is extremely important. If implemented poorly, these recommendations could discourage future mergers, because it is unlikely that any railroad would enter into a proposed merger if it were required, as a condition of the merger, to open its captive shippers to its competitors while the competitors, which would not be themselves merging, would not be required to open their captive shippers to competition. Such a scenario could freeze the railroad industry structure rather than permit it to seek its ultimate configuration.

PHA sees three ways in which this unintended consequence could be avoided.

First, the Board could condition a merger approval on opening captive shippers to competition, but withhold the effectiveness of that provision, under the Board's continuing oversight authority, until subsequent downstream mergers occurred and the open access requirement could be applied to all railroads at the same time. This, however, would delay the day when shippers were afforded competitive choices.

A second, and more attractive approach in terms of both merger policy and shippers' ability to enjoy competition, would be for the Board to establish a relatively short time window in which railroads could propose mergers, after which no merger applications would be accepted by the Board for an extended period of time, perhaps as much as twenty years. This would require all of the railroads to assess their ultimate position in the "final" industry structure and to present their proposed mergers to the Board within the "open window" time frame. The Board could then consider all of the merger proposals together and render a decision, with appropriate conditions assuring competitive access for all shippers, in a single comprehensive decision. This approach would prevent any merged railroad from being disadvantaged by having its merger proposal considered first and would eliminate the concept of "rounds" of mergers, replacing it with a comprehensive analysis and decision on the overall industry structure, including all downstream effects.

The third approach is the most attractive from a shipper perspective. Rather than requiring reciprocal switching or trackage rights to assure competitive access in major terminal areas, the Board could require that shipper access to the serving railroads be accomplished by a neutral switching railroad. Such a neutral switching railroad could be most effective in assuring quality, responsive service if it were accountable to a board comprised of local shippers and receivers served by the neutral switching railroad.

Port Issues

The Board asked for comments specifically addressing the issue of ports and how foreign ownership of a U.S. railroad might affect ports. Of particular importance to PHA is equity among ports.

The Port of Houston provides a nucleus for much of the industrial activity in the Houston region. The citizens of Houston and Harris County have made substantial investments over many decades in port facilities to support economic activity and job growth in the region, as have numerous industries with private docks and facilities located along the Houston Ship Channel. Most recently, the voters of Harris County authorized bonds for a portion of the costs associated with building a new $1.2 billion state-of-the-art container terminal.

The Port Authority believes that market forces should drive shippers' choices as to which ports they use for their import and export movements. These market-based decisions should not be affected by artificial preferences granted by railroad companies to specific ports.

The public interest is easily identified in this situation. It is reflected in the substantial public investments made in port infrastructure and services by the citizens of port cities. The public interest demands that shippers' choices of which ports to use not be made subject to the decisions of a railroad management.

Recommendations. The Board should require in its revised merger regulations that all merging railroads maintain strict neutrality between ports. This neutrality would require that railroads not give routing, service, rate, or promotional preferences to one port over another.

To accomplish this, PHA recommends that the Board require railroads to include in their merger application a comprehensive Ports Impact Statement and a Ports Service Plan. Implementation of the Ports Service Plan would be subject to oversight by both the Board, under its existing oversight authority, and a Ports Review Board comprised of representatives of the ports in the merged railroad's service area.

Summary

Competition. The Port of Houston Authority recommends that the Board's merger regulations affirmatively promote the preservation of railroad competition where it exists and the creation of railroad competition where it does not exist.

The Board should accomplish this preservation and creation of competition by using its authority to place conditions on its approval of mergers; the Board should apply those conditions thoughfully to prevent unintended consequences, such as requiring one railroad, but not the others, to permit competitive access to their captive shippers.

PHA recommends that the Board require all railroads intending to merge to participate in a comprehensive proceeding encompassing all of the proposed mergers and that the Board prohibit the railroads from proposing any other mergers for an extended number of years after the initiation of the comprehensive proceeding.

PHA also recommends that competitive service to shippers in major terminal areas be accomplished through a neutral switching carrier accountable to a board of railroad shippers in the terminal area.

Ports. The Port of Houston Authority further recommends that the Board's merger regulations affirmatively require that any merged railroad maintain complete neutrality between ports it serves, in its service, rates, and promotions.

To assure this neutrality, the Board's merger regulations should require merger applicants to submit a Ports Impact Statement and to develop a Ports Service Plan, which would be subject to oversight by both the Board and a Ports Review Board comprised of representatives of the ports in the merged railroad's service area.

CERTIFICATE OF SERVICE

I do hereby certify that copies of these Comments of the Port of Houston Authority have been served on all parties of record in STB Ex Parte No. 582 (Sub-No. 1) by first-class U.S. mail.

Richard J. Schiefelbein

May 15, 2000